BLANK

PAGE

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1965

No. [redacted] 63

BANK OF MARIN,
Petitioner,
vs.
JOHN M. ENGLAND, Trustee in Bankruptcy,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE PETITIONER

CARLOS R. FREITAS,
BRYAN R. MCCARTHY,
EDGAR B. WASHBURN,
FREITAS, ALLEN, MCCARTHY & BETTINI,
960 Fifth Avenue, San Rafael, California,
Counsel for Petitioner.

PERNAU-WALSH PRINTING CO., SAN FRANCISCO

BLANK

PAGE

Subject Index

Page

Opinions below 1

Jurisdiction 2

Statutes, federal rules and regulations involved 2

Question presented 2

Statement of the case 3

Summary of argument 6

Argument 9

I

The decision of the Court of Appeals, holding the bank liable for honoring checks of a depositor in good faith after the depositor filed a voluntary petition in bankruptcy where the bank had not been given notice, and had not otherwise obtained knowledge of the bankruptcy, applies portions of Sections 70a and 70d of the Bankruptcy Act in such a manner that they violate the due process clause of the Fifth Amendment of the Constitution 9

A. Due process requires that the bank be given notice of the bankruptcy of its depositor before it can be held liable for honoring checks of the depositor after bankruptcy 9

B. The bank cannot be compelled to pay the same debt twice 15

II

Courts repeatedly have held that equitable principles apply under the Bankruptcy Act to protect a bank honoring checks after a depositor's bankruptcy when the bank has no notice of the bankruptcy 16

A. Bankruptcy Act Section 70d does not apply to voluntary bankruptcies 16

Page

B. Prior to the enactment of Section 70d, courts of bankruptcy protected banks honoring a bankrupt depositor's checks after bankruptcy in good faith without notice 18

C. Well established equitable principles provide that the bank be protected in its payment 24

III

The negotiability provision of Section 70d(5) of the Bankruptcy Act protects a bank which honors checks of a bankrupt depositor in good faith without notice of the bankruptcy 26

Conclusion 32

Table of Authorities Cited

Cases Pages

Acme Harvester v. Beekman Lumber Company, 222 U.S. 300 (1911) 23

Andrews v. Partridge, 228 U.S. 479 (1913) 23

Citizens National Bank v. Johnson (6th Cir. 1923) 286 Fed. 527 .... 20, 22

Covey v. Town of Somers, 351 U.S. 141 (1956) 11

Edison Electric Company v. Tibbets (1st Cir. 1917) 241 Fed. 468 .... 20, 21

Everett v. Judson, 228 U.S. 474 (1913) 23

Fairbanks Steam Shovel Company v. Wills, 240 U.S. 642 (1916) 23

Frederick v. Fidelity Mut. Ins. Co., 256 U.S. 395 (1921) 13, 19, 20, 23

Pages

Glassell Development Co. v. Citizens National Bank, 191 Cal. 375, 216 Pac. 1012 (1923) 9, 15, 22

Hanover National Bank v. Moyses, 186 U.S. 181 (1902) 11
Harris v. Balk, 198 U.S. 215 (1905) 15
Huron Holding Corp. v. Lincoln Mine Operating Co., 312 U.S. 183 (1941) 15

In re Fuller (2nd Cir. 1923) 294 Fed. 71 .... 20, 21
In re Howe (D.C. Mass. 1916) 235 Fed. 908, aff'd sub. nom. 20, 21
In re LaPlume Condensed Milk Company (D.C.M.D. Penn. 1906) 145 Fed. 1013 20
In re Locust Building Co. Inc. (2nd Cir. 1924) 299 Fed. 756, cert. den. sub. nom. 19, 20
In re Peperall (2nd Cir. 1921) 271 Fed. 466 20
In re Raghman (8th Cir. 1910) 183 Fed. 913 20
In re Retail Stores Delivery Company (D.C.S.D.N.Y. 1935) 11 F.Supp. 658 20
In re Scranton Knitting Mills (D.C.M.D. Penn. 1937) 21 F. Supp. 227 .... 20, 21
In re Zotti (2nd Cir. 1911) 186 Fed. 84, cert. den. sub. nom. 20, 21

Jones v. Springer, 226 U.S. 148 (1912) 13, 19

Keighley v. American Trust Co., 265 U.S. 590 .... 19, 20

Lambert v. California, 355 U.S. 225 (1957) 12, 13
Local Loan Company v. Hunt, 292 U.S. 234 (1934) 24
Louisville Joint Stock Bank v. Radford, 295 U.S. 555 (1935) 11

McIntosh v. Funge, 128 Cal. App. 70, 16 P. 2d 1006 (1932) 5
Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306 (1949) 6, 11, 12, 13, 14

New York County Nat. Bank v. Massey, 192 U.S. 138 (1903) 6, 9, 15, 22
New York v. New York N.H. & H.R. Co., 344 U.S. 293 (1953) 6, 12

Painter v. Bergland, 31 Cal. App. 2d 63, 87 P. 2d 360 (1939) 5

Pages

Pepper v. Litton, 308 U.S. 295 (1939) 24

Rosenthal v. Guaranty Bank and Trust Company (D.C. La. 1956) 139 F.Supp. 730 .... 29, 30, 31

Schram v. Spivak (D.C.E.D. Mich. 1946) 68 F.Supp. 451 5
Schroeder v. City of New York, 371 U.S. 208 (1962) 11
Securities and Exchange Commission v. United States Realty and Improvement Company, 310 U.S. 434 (1934) 24
Stevens v. Bank of Manhattan Trust Company (D.C.S.D. N.Y. 1931) 11 F.Supp. 409 .... 20, 21

Tucker v. Nicholson, 12 C. 2d 427, 84 P. 2d 1045 (1938) .. 5

Union Tool v. Farmers, etc. National Bank, 192 Cal. 40, 218 Pac. 424 (1923) 9
United States v. Rumely, 345 U.S. 41 (1952) 18

Walker v. City of Hutchinson, 352 U.S. 112 (1950) 11
Watson v. European American Bank, 223 U.S. 718 .... 20, 21
Weaver v. Bank of America, 59 C. 2d 428, 380 P. 2d 644 (1963) 15, 22
Western Union Telegraph Co. v. Pennsylvania, 368 U.S. 71 (1961) 6, 15
Wright v. Mountain Trust Bank, 300 U.S. 440 (1936) 18
Wuchter v. Pizzutti, 276 U.S. 13 (1928) 14

Zavelo v. Reeves, 227 U.S. 625 (1913) 23

Statutes

Bankruptcy Act:
Section 2 (52 Stat. 842 (1938), 11 U.S.C. 11(a)) 24
Section 2(a) (52 Stat. 842 (1938), 11 U.S.C. 11(a)) .. 4
Section 18(f) (73 Stat. 109 (1959), 11 U.S.C. 41(f)) 2, 7, 17
Section 24 (66 Stat. 423 (1952), 11 U.S.C. 47) 5
Section 24(c) (66 Stat. 423 (1952), 11 U.S.C. 47(c)) .. 2
Section 25 (66 Stat. 424 (1952), 11 U.S.C. 48) 5
Section 39(c) (74 Stat. 528 (1960), 11 U.S.C. 67(c)) .. 5
Section 60 (64 Stat. 24 (1950), as amended, 11 U.S.C. 96) 25, 26, 28
Section 67 (66 Stat. 427 (1952), 11 U.S.C. 107) 26, 28

Pages
Section 70a (52 Stat. 879 (1938), as amended, 11 U.S.C. 110(a)) 2, 6, 8, 9, 10, 16, 18
Section 70d (52 Stat. 881 (1938), 11 U.S.C. 110(d))........................... 2, 6, 7, 8, 9, 10, 16, 17, 18, 19, 27
Section 70d(5) 8, 26, 27, 28, 30, 31
Section 102 (11 U.S.C. 502) 29

California Code of Civil Procedure, Section 709 4

28 U.S.C. 1254(1) 2

Constitutions

United States Constitution:
Article I, Section 8, Chapter 4 11
Fifth Amendment 2, 11

Rules

Federal Rules of Civil Procedure, Section 69 5

Texts

4 Collier on Bankruptcy, Section 70.67, pp. 1499, 1500 19

McLaughlin, 40 Harv. L. Rev. 583, 614 19

Miscellaneous

House Report 241 on H. R. 4692, 86 Cong. 1st Sess. (1959) 1, 2 17

Analysis of H.R. 1-2889, 74 Cong. 2d Sess. (1936), 229-230 19

BLANK

PAGE

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1965

No. 950

BANK OF MARIN, *Petitioner*, vs. JOHN M. ENGLAND, Trustee in Bankruptcy, *Respondent*.	

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The memorandum opinion of the District Court for the Northern District of California, Southern Division (R99-100) and the opinion of the referee in bankruptcy (R42-43) are unreported. The opinion of the Court of Appeals for the Ninth Circuit is reported at 352 F. 2d 186 (1965).

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was made and entered on October 28, 1965. The Petition for Writ of Certiorari was filed on January 26, 1966, and granted on February 21, 1966. The jurisdiction of this Court is conferred by Bankruptcy Act section 24(c), 66 Stat. 423 (1952), 11 U.S.C. 47(c); and 28 U.S.C. 1254(1).

STATUTES, FEDERAL RULES AND REGULATIONS INVOLVED

The applicable portions of the fifth amendment of the United States Constitution; Bankruptcy Act section 18(f), 73 Stat. 109 (1959), 11 U.S.C. 41; Bankruptcy Act section 70a, 52 Stat. 879 (1938) as amended, 11 U.S.C. 110(a); and Bankruptcy Act section 70d, 52 Stat. 881 (1938), 11 U.S.C. 110(d) are set forth in the appendix.

QUESTION PRESENTED

Is a bank which honored checks of a depositor after the depositor had filed a voluntary petition in bankruptcy, where the bank had no notice whatsoever of the bankruptcy proceeding, liable to the trustee in bankruptcy for the amount of the checks paid?

STATEMENT OF THE CASE

The facts are not in dispute. Between August 27, 1963, and September 17, 1963, Marin Seafoods, Inc. drew and delivered five checks, totaling $2,312.82, in favor of Eureka Fisheries, Inc. on its commercial account with the petitioner Bank of Marin, San Rafael, California. (R46.)

On September 26, 1963, before the checks were presented to the Bank of Marin for payment, Marin Seafoods filed a voluntary petition in bankruptcy in the United States District Court for the Northern District of California, Southern Division, San Francisco, California. (R44.) John M. England was appointed receiver on September 30, 1963, and acted as such until October 20, 1963, at which time he became trustee for the bankrupt. (R45.)

On October 2, 1963, the checks which Marin Seafoods had drawn and delivered to Eureka Fisheries prior to the filing of the petition in bankruptcy were duly presented for payment by Eureka Fisheries to the Bank of Marin. (R46.) Sufficient funds were on deposit and the bank in good faith honored the checks. (R8.) At the time the bank paid the checks it had received no notice, and had not otherwise obtained knowledge of the filing of the voluntary petition in bankruptcy by Marin Seafoods. (R47.) The Bank of Marin was not informed of the pending bankruptcy proceedings until the next day, October 3, 1963, when it received a letter dated October 2, 1963, from the receiver. (R46, 47.)

On November 27, 1963, the trustee applied to the referee for a turnover order pursuant to section 2(a) of the Bankruptcy Act, 52 Stat. 842 (1938), 11 U.S.C. 11(a), seeking to require the bank to pay over to the trustee a sum of money equivalent to the sum it paid Eureka Fisheries on October 2, 1963. (R1-3.) In the alternative, the trustee sought the same relief against Eureka Fisheries. Immediately, an order to show cause was issued by the referee ordering the Bank of Marin and Eureka Fisheries to show why the relief prayed for by the trustee should not be granted. (R3-4.)

After the hearing on the order to show cause, the referee held that the Bank of Marin and Eureka Fisheries were jointly liable to the trustee for the sum of $2,312.82, the amount paid by the Bank of Marin to Eureka Fisheries. (R47, 48.) Subsequently, Eureka Fisheries paid the total amount of $2,312.82 to the trustee and filed with the bankruptcy court, and served upon the bank, a notice of payment and demand for contribution pursuant to California Code of Civil Procedure section 709, thereby entitling Eureka Fisheries to the remedy of execution to recover from the bank one-half the amount Eureka Fisheries paid on the joint judgment.[1] (R54, 55.)

---

[1]California Code of Civil Procedure section 709 provides: "*Party Who Pays More Than His Share May Compel Contribution.* When property, liable to an execution against several persons, is sold thereon, and more than a due proportion of the judgment is satisfied out of the proceeds of the sale of the property of one of them, or one of them pays, without a sale, more than his proportion, he may compel contribution from the others; . . . In such case, the person so paying or contributing is entitled to the benefits of the judgment, to enforce contribution or repayment, if, within ten days after

The Bank of Marin petitioned for review of the referee's order pursuant to section 39(c) of the Bankruptcy Act, 74 Stat. 528 (1960), 11 U.S.C. 67(c). (R50, 51.) The District Court affirmed the referee's decision and the bank then appealed that decision in accordance with section 24, (66 Stat. 423 (1952), 11 U.S.C. 47) and section 25, (66 Stat. 424 (1952), 11 U.S.C. 48) of the Bankruptcy Act. (R99-105.) The Court of Appeals for the Ninth Circuit made and entered its judgment affirming the decision of the District Court on October 28, 1965. (R105-117.)

The bank has taken the position at each successive stage of these proceedings that it is not liable to a trustee in bankruptcy when, in good faith, and without notice of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the filing of a voluntary petition. However, the referee, the District Court and the Court of Appeals, after having considered the question, have held that the lack of notice and the fact that the payments were made in good faith afford no protection to the Bank of Marin. (R47, 99, 100, 105-116.)

---

payment, he files with the clerk of the court where the judgment was rendered, notice of his payment and claim to contribution or repayment. Upon a filing of such notice, the clerk must make an entry thereof in the margin of the docket."

This section enables a joint judgment debtor, who pays more than his portion of the judgment, to use the judgment to enforce contribution from his co-debtor by immediate execution without the necessity of further proceedings. *Tucker v. Nicholson,* 12 C. 2d 427, 84 P. 2d 1045 (1938); *Painter v. Bergland,* 31 Cal. App. 2d 63, 87 P. 2d 360 (1939); *McIntosh v. Funge,* 128 Cal. App. 70, 16 P. 2d 1006 (1932). This procedure is applicable in the federal courts. Federal Rules of Civil Procedure section 69. *Schram v. Spivak* (D. C. E. D. Mich. 1946) 68 F. Supp. 451.

SUMMARY OF ARGUMENT

I

The decision of the Court of Appeals, holding that sections 70a and 70d of the Bankruptcy Act impose liability upon a bank which, after the filing of a voluntary petition in bankruptcy by a depositor, honors checks of the depositor in good faith without notice of the bankruptcy, renders those sections violative of the due process clause of the fifth amendment of the United States Constitution.

Due process requires that a bank be given reasonable notice of the bankruptcy of one of its depositors before it can be held responsible for honoring checks of that depositor in good faith. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1949); *New York v. New York N.H. & H.R. Co.*, 344 U.S. 293 (1953).

The relationship between a bank and its depositor is that of debtor and creditor giving rise to an obligation on the part of the bank to discharge its indebtedness by honoring such checks as its depositor may draw upon it. *New York County Nat. Bank v. Massey*, 192 U.S. 138 (1903). By holding that the Bank of Marin must pay to the trustee of its bankrupt depositor, Marin Seafoods, a sum equivalent to the sum that it paid in honoring the checks of Marin Seafoods, the Court of Appeals is compelling the bank to satisfy the same debt twice, thereby violating the Constitutional prohibition against forcing a person to pay the same obligation more than once. *Western Union Telegraph Co. v. Pennsylvania*, 368 U.S. 71 (1961).

II

Prior to 1938, there was no provision in the Bankruptcy Act dealing with the protection of good faith transfers of the bankrupt's property after bankruptcy. However, a considerable body of law evolved, based upon fundamental concepts of equity and justice, which protected innocent parties who dealt bona fides with the bankrupt's property. It was well established that banks which honored checks of a bankrupt depositor after bankruptcy in good faith without notice of the bankruptcy were protected in such payment.

In 1938, section 70d was added to the Bankruptcy Act as a part of the Chandler Amendment. Section 70d set forth in the act for the first time specific restrictions upon good faith transfers of the bankrupt's property after bankruptcy. The only transfers that were protected were those occurring between the time of the filing of the petition and adjudication or before a receiver took possession of the bankrupt's property.

In 1959, Bankruptcy Act section 18g was amended (renumbered as section 18f) to make adjudication automatic upon the filing of a voluntary petition. The amendment eliminated section 70d from application to voluntary bankruptcies by removing the interval during which that section was effective. Consequently, there is no longer any provision in the Bankruptcy Act limiting those situations where protection will be afforded good faith transfers of the bankrupt's property after the filing of a voluntary petition. The problem of determining which transactions are to be protected is again left up to courts which are free to

apply well established equitable principles to protect the Bank of Marin.

By relieving the Bank of Marin of liability, due process can be accorded the bank and the constitutional limitations of the Court of Appeals' interpretation of sections 70a and 70d of the Bankruptcy Act can be avoided.

III

Section 70d(5) of the Bankruptcy Act provides in part that ". . . nothing in this title shall impair the negotiability of currency or negotiable instruments". The broad language of that proviso protects transfers of negotiable instruments occurring before and after adjudication if the imposition of liability upon any party to the transaction would impair the negotiability of the instrument.

To impose liability upon a drawee bank honoring checks of a bankrupt depositor in good faith without notice of the bankruptcy, impairs the negotiabiiity of the checks. The only means by which a bank could avoid the consequences of the Court of Appeals' decision would be to delay acceptance of a check until such time as the bank completed the impossible task of ascertaining whether the depositor had filed a petition in bankruptcy in any district in the country. This would not only violate the bank's legal obligation to its depositor to honor the checks upon presentment, but would destroy the freedom with which checks flow in the commercial world and would limit their usefulness as a substitute for money.

ARGUMENT

I

THE DECISION OF THE COURT OF APPEALS, HOLDING THE BANK LIABLE FOR HONORING CHECKS OF A DEPOSITOR IN GOOD FAITH AFTER THE DEPOSITOR FILED A VOLUNTARY PETITION IN BANKRUPTCY WHERE THE BANK HAD NOT BEEN GIVEN NOTICE, AND HAD NOT OTHERWISE OBTAINED KNOWLEDGE OF THE BANKRUPTCY, APPLIES PORTIONS OF SECTIONS 70a AND 70d OF THE BANKRUPTCY ACT IN SUCH A MANNER THAT THEY VIOLATE THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT OF THE CONSTITUTION.

A. Due process requires that the bank be given notice of the bankruptcy of its depositor before it can be held liable for honoring checks of the depositor after bankruptcy.

Prior to the intervention of bankruptcy, the relationship between the Bank of Marin and its depositor, Marin Seafoods, was that of debtor and creditor, giving rise to an obligation on the part of the bank to discharge its indebtedness by honoring such checks as its depositor drew upon it. *New York County Nat. Bank v. Massey,* 192 U.S. 138 (1903); *Union Tool v. Farmers, etc. National Bank,* 192 Cal. 40, 218 Pac. 424 (1923); *Glassell Development Co. v. Citizens National Bank,* 191 Cal. 375, 216 Pac. 1012 (1923).

When Marin Seafoods' checks were duly presented for payment on October 2nd, there were sufficient funds on deposit to its credit with the Bank of Marin and the bank in good faith proceeded to pay the checks (R8, 46, 47.) The Court of Appeals, nevertheless, has held that the Bank of Marin is liable to the trustee in bankruptcy for an amount equivalent to the sum it paid in honoring the checks.

The decision of the Court of Appeals turned upon its interpretation of the effect of Bankruptcy Act section 70a in conjunction with Bankruptcy Act section 70d. It held that section 70a vested the trustee in bankruptcy, by operation of law, with the title of the bankrupt to its bank deposits as of the date of the filing of the voluntary petition. Therefore, the Court reasoned, the Bank of Marin must be liable to the trustee for the sums it paid in honoring the checks after the bankruptcy of its depositor, Marin Seafoods, even though it had no notice of the bankruptcy and was acting in good faith. In so doing, the Court decided that the only transactions that are protected after bankruptcy are those coming within the purview of Bankruptcy Act section 70d and that nothing in that section afforded the bank relief.

Although it was conceded by the Court of Appeals that no notice was given to the bank and that it had not otherwise acquired knowledge of the bankruptcy, the Court imposed liability upon the bank. (R106.) It stated that the bank was not entitled to any notice beyond the caveat that accompanies the filing of a voluntary petition. It is the position of the petitioner, Bank of Marin, that such an application of Bankruptcy Act would render sections 70a and 70d[2] violative of the due process clause of the Fifth Amendment of the United States Constitution.

---

[2]The applicable portions of Bankruptcy Act sections 70a, 52 Stat. 879 (1938) as amended, 11 U.S.C. 110(a), and 70d, 52 Stat. 881 (1938), 11 U.S.C. 110(d), are set forth in the Appendix.

The exercise of the constitutional grant of power to Congress to legislate on the subject matter of bankruptcies (U.S. Constitution, article I, section 8, chapter 4) is limited by the due process clause of the Fifth Amendment. *Louisville Joint Stock Land Bank v. Radford,* 295 U.S. 555 (1935); *Hanover National Bank v. Moyses,* 186 U.S. 181 (1902). Congress may prescribe regulations concerning bankruptcies, but it may not dictate regulations that are so grossly unreasonable as to be incompatible with fundamental law and due process. *Hanover National Bank v. Moyses,* 186 U.S. 181 (1902); *Louisville Joint Stock Bank v. Radford,* 295 U.S. 555 (1935).

It is no longer open to question that an elementary and fundamental requirement of due process is that deprivation of property by adjudication be preceded by notice and an opportunity for hearing. *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306 (1949). The principles enunciated by this Court in *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306 (1949), regarding notice have been consistently followed and applied. It is necessary that reasonable notice of a condemnation action be given a landowner prior to the time his rights are affected, even though the governmental authority has the absolute right to condemn. *Walker v. City of Hutchinson,* 352 U.S. 112 (1950); *Schroeder v. City of New York,* 371 U.S. 208 (1962). Similarly, due process requires that notice of foreclosure of a tax lien be given the defaulting taxpayer upon whose real property the tax has become a lien. *Covey v. Town of Somers,* 351

U.S. 141 (1956). In a like manner, it is held that beneficiaries of a common trust fund be given notice of all proceedings which affect their interests in order to satisfy due process. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1949).

More specifically, this Court held in *New York v. New York N. H. and H. R. Co.*, 344 U.S. 293 (1953), that a city having a lien upon specific real property of a railroad reorganizing under section 77 of the Bankruptcy Act must be given notice of those stages of the proceedings where its rights would be affected consistent with the requirements established in *Mullane*. The principles relied upon in the *New York v. New York N. H. and H. R. Co.* case apply with equal force to any person whose property rights will be adversely affected by bankruptcy.

Where notice is required by due process, it must be given prior to the time when property rights are disturbed. *Lambert v. California*, 355 U.S. 225 (1957).

> ". . . Notice is required before property interests are disturbed, before assessments are made, before penalties are assessed. Notice is required in a myriad of situations where a penalty or forfeiture might be suffered for mere failure to act. Recent cases illustrating the point are *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306; *Covey v. Town of Somers*, 351 U.S. 141; *Walker v. Hutchinson City*, 352 U.S. 112. These cases involved only property interests in civil litigation. But the principle is equally appropriate where a person, wholly passive and unaware of any wrongdoing, is brought to the bar of justice for con-

demnation in a criminal case." (*Lambert v. California,* 355 U.S. 225 at p. 228.)

The Court of Appeals stated that the requirements of due process have been met since the Bank of Marin received notice of the hearing on the turnover order. The position of that Court in this regard is not well taken. If the Court is correct in holding that adjudication has the effect of shifting the bank's obligation to pay from its depositor to the trustee as of the date of the filing of the petition, the bank must receive reasonable notice of that event so that it may decide whether or not to honor the checks as they are presented with full knowledge of the possible consequences. Notice of any subsequent proceeding, such as the hearing on the turnover order, is obviously ineffectual to give the bank an opportunity to protect itself by refusing to honor the checks.

The type of notice that must be given in order to satisfy due process is that which is reasonably calculated, under all the circumstances, to apprise interested parties of the pending action. *Mullane v. Central Hanover Trust & Bank Co.,* 339 U.S. 306 (1949). If the act of filing a voluntary petition is notice of any kind, it is certainly not reasonably calculated to put the bank on notice of its filing. Although the filing of the petition is often considered to be caveat to the whole world, it has been stated that the caveat is not equivalent to effective notice in many situations. *Jones v. Springer,* 226 U.S. 148 (1912); *Frederick v. Fidelity Mut. Ins. Co.,* 256 U.S. 395 (1921).

The reasonableness and hence the constitutional validity of any given mode of notice is determined by balancing the certainty that the notice will reach those affected against the feasibility of giving such notice. *Mullane v. Central Hanover Trust & Bank Co.,* 339 U.S. 306 (1949). The trustee (initially the receiver) knew of the existence and the location of the Marin Seafoods deposit with the Bank of Marin. Under the circumstances it would not have been burdensome in any respect to telephone or to mail notice to the bank. As stated in *Mullane* (339 U.S. 306, 318 (1949):

> ". . . Where the names and postoffice addresses of those affected by a proceeding are at hand, the reasons disappear for resort to means less likely than the mails to apprise them of its pendency."

The trustee made much out of the argument that the bank could have discovered that one of its depositors had filed a petition in bankruptcy by searching the various legal newspapers that are independently published. However, it is a practical impossibility to accomplish such a task. While in this case the petition was filed in the adjoining county of San Francisco, to be fully protected the bank would have to keep itself advised momentarily of every bankruptcy filing in every district in the country. Moreover, the fact that the bank might have acquired knowledge is not a substitute for the failure of the trustee to fulfill the requisites of due process by providing reasonable notice. *Wuchter v. Pizzutti,* 276 U.S. 13 (1928).

B. The bank cannot be compelled to pay the same debt twice.

Due process not only requires that a person receive adequate notice prior to the time his property interests are disturbed, but it also protects a person from paying the same debt more than once. *Western Union Telegraph Co. v. Pennsylvania,* 368 U.S. 71 (1961); *Harris v. Balk,* 198 U.S. 215 (1905); *Huron Holding Corp. v. Lincoln Mine Operating Co.,* 312 U.S. 183 (1941).

The bank was obligated to discharge its indebtedness to Marin Seafoods by honoring the checks which were drawn upon it. *New York County Nat. Bank v. Massey,* 192 U.S. 138 (1903); *Glassell Development Co. v. Citizens National Bank,* 191 Cal. 375, 216 Pac. 1012 (1923). Based upon the facts that were known to the bank at the time the checks were presented for payment on October 2, the bank would have been liable for damages to its depositor had it not fulfilled this obligation. *Weaver v. Bank of America,* 59 C. 2d 428, 380 P. 2d 644 (1963). The decision of the Court of Appeals, ordering the bank to pay an equivalent sum to the trustee, compels the bank to pay the same debt twice.

The Court discounted the double payment problem by taking the position that as of the moment of the filing of the voluntary petition, the bank's duty with regard to the deposit was shifted from its depositor to the trustee, and consequently, the bank, in honoring the checks was not satisfying an obligation. The Court did not face up to the basic issue presented, that is,

can the bank's obligation to its depositor be transferred to the trustee without giving the bank notice of that fact, and that lacking such notice, can the bank be held to dual liability if it honors its depositor's checks in good faith without notice? The imposition of such a burden upon the bank violates the basic precepts of due process that have been long established by this Court. The right to notice and to protection from double payment are two of the cornerstones of due process. Lack of these cornerstones constitutes an absence of that fundamental fairness essential to the very concept of justice.

II

COURTS REPEATEDLY HAVE HELD THAT EQUITABLE PRINCIPLES APPLY UNDER THE BANKRUPTCY ACT TO PROTECT A BANK HONORING CHECKS AFTER A DEPOSITOR'S BANKRUPTCY WHEN THE BANK HAS NO NOTICE OF THE BANKRUPTCY.

A. Bankruptcy Act section 70d does not apply to voluntary bankruptcies.

The Court of Appeals held that section 70a vested the trustee with the title of the bankrupt to its deposit as of the date of the filing of the petition and that honoring a prior transfer of any portion of that deposit after bankruptcy could be valid against the trustee only if it was authorized by section 70d. Since that section makes no provision for transfers taking place after adjudication, the Court determined that any interpretation of the Act that would protect the Bank of Marin would conflict with section 70d and was therefore precluded.

However, section 70d has no application to voluntary proceedings. The introductory clause of that section which provides that: "After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—", clearly limits section 70d's application to transactions occurring during the interval between the filing of a petition and before adjudication or before the receiver takes possession of the property of the bankrupt. If there is no such interval, section 70d does not apply.

Prior to 1959, there was a lapse of time between the filing of a petition and the adjudication of bankruptcy in both voluntary and involuntary cases during which transfers falling within the purview of section 70d were protected. However, in 1959, section 18g of the Act was amended and renumbered as section 18f. Section 18f made adjudication automatic on the filing of a voluntary petition thereby eliminating the interval that previously existed. With the removal of this time period, there can be no instance where section 70d would apply in a voluntary bankruptcy since by its terms adjudication is the cutoff date.[3] The

[3]It was not the intent of Congress in enacting section 18f to effect any change in the substance of section 70d or to deny its application to a voluntary bankruptcy. Section 18f was designed to bring about a procedural change by making adjudication automatic upon the filing of a voluntary petition. Under the prior section (18g) the district judge was required to hear all voluntary petitions and to either make the adjudication or dismiss the petition. Since there were no issues to be presented, adjudication became a matter of course. By making adjudication automatic, Congress intended to remove the burden of hearing all the petitions from the district judge. (See: House Report 241 on H. R. 4692, 86 Cong. 1st Sess. (1959) 1, 2). No consideration was given

result is the complete elimination from the Bankruptcy Act of any provision dealing with the protection of bona fide transfers after the filing of a voluntary petition.

B. Prior to the enactment of section 70d, courts of bankruptcy protected banks honoring a bankrupt depositor's checks after bankruptcy in good faith without notice.

Petitioner does not contend that the Bankruptcy Act specifically provides that the bank receive notice of the filing of a petition in bankruptcy or of the adjudication of a depositor. It is clear that there is no such provision in the Act. However, it is a cardinal principle long established by this Court that a statute will be interpreted so as to avoid possible constitutional limitations. *United States v. Rumely,* 345 U.S. 41 (1952); *Wright v. Mountain Trust Bank,* 300 U.S. 440 (1936). The Bankruptcy Act can be construed so that it does not violate the due process limitations previously discussed by either implying the requirement of notice, or, by holding that its provisions do not impose liability upon a bank under the facts presented here.

Section 70d was added to the Bankruptcy Act as a part of the major revision brought about by the enactment of the Chandler Act in 1938. Prior to that time, there had been no similar provision limiting the effect of 70a. There was, however, a considerable body of law compelled by considerations of justice and

---

to the fact that such an amendment had the additional and more important consequence of eliminating protection for all transactions involving voluntary bankruptcies after the date of the filing of the petition.

equity that protected those who dealt in good faith with the bankrupt after bankruptcy. Section 70d was designed to eliminate the confusion that arose because of inconsistent judicial decisions. Its enactment was intended to set forth in an orderly fashion those good faith transfers where protection would be afforded. It was not, however, intended to codify all those transactions which were previously protected. (See: Analysis of H.R. 12889, 74 Cong. 2d Sess. (1936) 229-230; *McLaughlin,* 40 Harv. L. Rev. 583, 614; 4 *Collier on Bankruptcy,* Sec. 70.67, pages 1499, 1500.)

With the removal of section 70d from application to voluntary bankruptcies, the status of the law relating to bona fide transfers after bankruptcy is the same as it was prior to 1938. Notwithstanding the fact that the filing of the petition was said to be "caveat to all the world, and in effect an attachment and injunction," the courts prior to 1938, made exceptions to the doctrine where its application would work a hardship on an innocent party, who, following the inception of bankruptcy, dealt with the bankrupt on a bona fide basis for a present consideration. *Jones v. Springer,* 226 U.S. 148 (1912); *Frederick v. Fidelity Insurance Company,* 256 U.S. 395 (1921); *In re Locust Building Co. Inc.* (2nd Cir. 1924) 299 Fed. 756, certiorari denied sub. nom. *Keighley v. American Trust Co.,* 265 U.S. 590. It was recognized that where innocent parties were concerned, the mere filing of the petition gave rise to no notice that would put such persons on guard. *Frederick v. Fidelity Insurance Co.,* 256 U.S. 395 (1921); *In re Locust Building Co. Inc.* (2nd

Cir. 1924) 299 Fed. 756, certiorari denied sub. nom. *Keighley v. American Trust Co.,* 265 U.S. 590; *In re Raghman* (8th Cir. 1910) 183 Fed. 913; *Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527; *In re LaPlume Condensed Milk Company* (D.C.M.D. Penn. 1906) 145 Fed. 1013.

Cash sales were protected (*In re Peperall* (2nd Cir. 1921) 271 Fed. 466), as were payments by insurance companies in the ordinary course of business. (*Frederick v. Fidelity Insurance Company,* 256 U.S. 395 (1921).) Moreover, banks which honored checks of a depositor after bankruptcy, in good faith and without notice of the proceedings, were protected as against a subsequent claim to the money by the trustee. *In re Retail Stores Delivery Company* (D.C. S.D.N.Y. 1935) 11 F.Supp. 658; *Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527; *In re Fuller* (2nd Cir. 1923) 294 Fed. 71; *In re Zotti* (2nd Cir. 1911) 186 Fed. 84, certiorari denied sub. nom. *Watson v. European American Bank,* 223 U.S. 718; *Stevens v. Bank of Manhattan Trust Company* (D.C. S.D.N.Y. 1931) 11 F.Supp. 409; *In re Scranton Knitting Mills* (D.C.M.D. Penn. 1937) 21 F.Supp. 227; *In re Howe* (D.C. Mass. 1916) 235 Fed. 908, aff'd sub. nom. *Edison Electric Company v. Tibbets* (1st Cir. 1917) 241 Fed. 468.

Various reasons were adopted by the courts for not imposing liability against banks under such circumstances. It was said that the adage that "the filing of a petition is caveat to all the world," was not intended to apply to banks which honestly paid checks of a

depositor without notice of the bankruptcy. *In re Fuller* (2nd Cir. 1923) 294 Fed. 71; *In re Zotti* (2nd Cir. 1911) 186 Fed. 84, certiorari denied sub. nom. *Watson v. European American Bank,* 223 U.S. 718. The fact that the bank had an obligation to honor its depositors' checks was also held to support such a conclusion. *Stevens v. Bank of Manhattan Trust Company* (D.C.S.D.N.Y. 1931) 11 F.Supp. 409; *In re Howe* (D.C. Mass. 1916) 235 Fed. 908, aff'd sub. nom. *Edison Electric Company v. Tibbets* (1st Cir. 1917) 241 Fed. 468. Moreover, the fact that it was in the best interests of the free play of commerce was said to support a decision that a bank should not be held liable for honoring checks in good faith after bankruptcy. *In re Scranton Knitting Mills* (D.C.M.D. Penn. 1937) 21 F.Supp. 227.

However, the ground most frequently relied upon was the inequity of a contrary result. The courts recognized that it was virtually impossible for a bank to acquire notice of the bankruptcy of a depositor in order to protect itself against liability. The following statement from one of the earlier cases is typical.

> ". . . Its effect would be that the bank could not protect itself against liability to a trustee of bankruptcy subsequently appointed on account of payments made in good faith and in the regular course of business and in ignorance of the bankruptcy proceedings—except through the impossible course of keeping itself advised, not only daily, but momentarily, of the filing of petitions for adjudication of bankruptcy against depositors in any competent jurisdiction. In our opinion the bankruptcy works no such result. True, broadly

> speaking the adjudication when made relates back to the commencement of the bankruptcy proceedings for the purpose of adjudicating rights and equities generally (citing cases). But we think that both on principle and authority the rule referred to does not make the banker liable for good faith payments to third persons made before adjudication upon depositors' checks in the regular course of business and without the knowledge or notice of bankruptcy." *(Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527 at 528.)

The dilemma in which the bank is placed as expressed in the opinion set forth above is compounded by the fact that the bank owes an obligation to its depositors to honor their checks when they are presented for payment. (See: *New York County Nat. Bank v. Massey,* 192 U.S. 138 (1903); *Glassell Development Co. v. Citizens National Bank,* 191 Cal. 375, 216 Pac. 1012 (1923); *Weaver v. Bank of America,* 59 C.2d 428, 380 P.2d 644 (1963).) This was recognized by the Ninth Circuit in this very case:

> "The bank's dilemma is real since it is under a duty to depositors to honor checks which are validly drawn; at the same time there is always a possibility that the depositor, without the knowledge of the bank, has become the subject of bankruptcy proceedings. The hardship to the bank in keeping itself apprised of developments in the bankruptcy court is contrasted with the relatively light burden that a notice requirement would place upon the trustee. The trustee or receiver, upon filing, is informed of the bankrupt's accounts and deposits; and notification by him to the bank would be relatively simple." (R111.)

The fact that many of the cases discussed above dealt with situations where the transaction occurred prior to adjudication is not a distinguishing factor. Although the enactment of section 18f in 1959 made adjudication automatic upon the filing of a voluntary petition, the doctrine of "relation back", which has been consistently applied by the courts in the past, effected the same result by holding that the trustee's title vested as of the date of the petition. See: ***Everett v. Judson,*** 228 U.S. 474 (1913); ***Andrews v. Partridge,*** 228 U.S. 479 (1913); ***Acme Harvester v. Beekman Lumber Company,*** 222 U.S. 300 (1911); ***Zavelo v. Reeves,*** 227 U.S. 625 (1913); ***Fairbanks Steam Shovel Company v. Wills,*** 240 U.S. 642 (1916).

More importantly, the constitutional objections that have previously been discussed apply with equal force to the lack of notice that accompanies adjudication as to the insufficiency of notice attendant to the filing of a voluntary petition. Adjudication does not make the filing any more notorious. That fact was recognized in ***Frederick v. Fidelity Mutual Insurance Company,*** 256 U.S. 395, 398-399 (1921). The ***Frederick*** case is particularly significant since it held that a transfer made after adjudication was valid where no notice of the filing of the petition or of adjudication had been given. In ***Frederick,*** the bankrupt owned a life insurance policy which had a cash surrender value at the time the petition was filed. The bankrupt died and the insurance company paid the full value of the policy to the beneficiary. The company at no time prior to payment had notice of the filing of the petition or of the adjudication. The trustee then filed suit to recover

the surrender value of the policy as of the date of adjudication, basing his claim on Bankruptcy Act section 70a. The Court, in holding that the company was not liable to the trustee unless it had been given notice, stated (at page 398):

> "It is not enough to sustain the trustee's claim to say that the filing of the petition in bankruptcy was a caveat to all the world, and in effect an attachment and injunction, and that, on adjudication, title to the bankrupt's properties became vested in the trustee. . . ."

With the practical elimination of section 70d from application to voluntary proceedings, there are no limitations set forth in the Act defining the limits of protection which conflict with the results of the earlier decisions. The numerous reasons that have constrained courts of bankruptcy in the past to exercise their equitable powers to protect good faith payments by a bank after bankruptcy are present here.

C. Well established equitable principles provide that the bank be protected in its payment.

Courts of bankruptcy are essentially courts of equity and may exercise broad equitable powers to protect hardship and unfairness. *Local Loan Company v. Hunt,* 292 U.S. 234 (1934); *Pepper v. Litton,* 308 U.S. 295 (1939); *Securities and Exchange Commission v. United States Realty and Improvement Company,* 310 U.S. 434 (1934); Bankruptcy Act section 2, 52 Stat. 842 (1938), 11 U.S.C. 11(a). The unfairness of the Court of Appeals' ruling is obvious. The Bank of Marin, which was under a legal obligation to honor

the checks of its depositor, Marin Seafoods, honored the checks in good faith. By so doing, the bank has been held liable to the trustee for a sum equivalent to that paid even though the bank had no knowledge of the bankruptcy. The only means by which the bank could have protected itself from being placed in this dilemma was to ascertain whether or not the depositor had filed a voluntary petition of bankruptcy in any District Court in the United States before it honored the checks. The very magnitude of such a task renders it impossible.

Opposed to the virtually impossible duty that is placed upon the bank, the trustee could easily have notified the bank by mail or by telephone of the fact that a voluntary petition had been filed. The bank account was listed in the schedules filed by the bankrupt and the name and address of the bank were readily available.

The inequity of the holding of the Court of Appeals is emphasized by the potential exposure to liability that is placed upon banks. Although this case involves only a few checks amounting to several thousand dollars, a similar situation involving many times that amount of money is not remote. In contrast to the virtually unlimited exposure placed upon banks, is the fact that the bankruptcy estate would be losing nothing if banks were protected. Any payment to a third party by the bankrupt which occurs so close to the moment of bankruptcy that the check is presented for payment after the filing of a voluntary petition would be a preference (Bankruptcy Act section 60, 64

Stat. 24 (1950), as amended, 11 U.S.C. 96) or a fraudulent transfer (Bankruptcy Act section 67, 66 Stat. 427 (1952), 11 U.S.C. 107) and recoverable by the trustee from the payee.

III

THE NEGOTIABILITY PROVISION OF SECTION 70d(5) OF THE BANKRUPTCY ACT PROTECTS A BANK WHICH HONORS CHECKS OF A BANKRUPT DEPOSITOR IN GOOD FAITH WITHOUT NOTICE OF THE BANKRUPTCY.

In holding that the bank is liable to the trustee for an amount equivalent to the sums it paid in honoring the checks of its bankrupt depositor, the Court of Appeals stated that the "negotiability" provision of Bankruptcy Act section 70d(5) does not apply. The Court put forward two reasons as justifying such a conclusion.

First, it stated that the introductory words to section 70d indicate that it applies only to transactions taking place during the interval between the filing of the petition and adjudication or the taking of possession by a receiver. Since in the case of a voluntary petition, there is no such interval, section 70d(5) was said to have no application.

The Court of Appeals ignored the plain meaning of the last sentence of section 70d(5) which reads, "Provided, however, that nothing in this title shall impair the negotiability of currency or negotiable instruments." That provision appears on its face to apply to all of Title 11 of the United States Code (the

Bankruptcy Act). It is not dependent upon any other provision of the Bankruptcy Act or the remainder of section 70d for its application. The fact that the other portions of section 70d do not apply to voluntary bankruptcies has no bearing on the effect of the negotiability proviso.

Secondly, the Court of Appeals stated that the negotiability clause did not afford protection to the bank since presentment of a check to the drawee bank for payment, and payment thereof, is not a technical negotiation. However, the negotiability proviso of section 70d(5) does not limit its application to parties to a negotiation or, for that matter, to a holder in due course. Protection is afforded to anyone whose relationship to a transaction involving a negotiable instrument is such that the negotiability of that instrument would be impaired if liability were imposed upon such person.

Negotiability gives the holder of a negotiable instrument maximum assurance that he will be able to collect on such document without any defenses being interposed. It is that characteristic which permits such documents to flow freely in the commercial world and to be utilized as a substitute for money. It is difficult to imagine a situation where the concept of negotiability is more seriously hampered by bankruptcy than by holding a drawee bank responsible for honoring checks of a bankrupt depositor in good faith without notice of the bankruptcy. The entire risk of loss in untold instances would be placed upon a bank which is the only party to such a transaction acting

in good faith, as a mere conduit for payment. On the other hand, the bankrupt is obviously aware of the ramifications of his act and the payee will generally be a preferred creditor (Bankruptcy Act section 60) or a fraudulent transferee (Bankruptcy Act section 67).

Moreover, the only means by which the bank could avoid the consequences of the Court of Appeals' decision would be to delay acceptance of a check until such time as it could be ascertained that the bank's depositor was not in bankruptcy. This would not only violate the bank's legal obligation to its depositor to honor the check upon presentment, but would also destroy the freedom with which checks flow in the commercial world and their usefulness as a substitute for money.

It is inconceivable that Congress, in enacting section 70d(5), intended to eliminate from its protective coverage the party that most frequently would be involved in the negotiation of checks, that is, the drawee bank. This is particularly true since the negotiability provision would afford little protection to the payee. Is it not more probable that Congress intended this exception primarily for the protection of banks upon whom the orderly flow of the country's money depends and to whom it is entrusted under Federal and State regulations?

The one other reported decision that has dealt with the issue presented in this petition adopted the reasoning set forth above and held that the negotiability provision of section 70d(5) protected a bank which

honored checks in good faith after the adjudication of bankruptcy of its depositor without notice. *Rosenthal v. Guaranty Bank & Trust Co.* (D.C. La. 1956) 139 F.Supp. 730.[4]

The reasoning of the *Rosenthal* decision is best set forth in the following quotation:

> "The Trustee particularly directs the Court's attention to Subparagraph (5) of Title 11 U.S.C.A. Section 110, subdivision d, which he says plainly and expressly states that except as provided in subdivision d and in subdivision g of Section 44 (which latter subdivision relates to real estate and has no bearing here), no other transfer after the date of the bankruptcy shall be valid against the Trustee, and of course, he argues, the only exceptions stated in subdivision d are that the payments must be made both before adjudication and without notice of the pending proceedings.
>
> "This argument is not without merit and were it not for the fact that there is appended to that Section the proviso 'that nothing in this title shall impair the negotiability of currency or negotiable instruments', we would be inclined to agree. Since no court decision has been called to our

[4]Although the *Rosenthal* case arose under a voluntary petition for corporate reorganization pursuant to Chapter X of the Bankruptcy Act, Chapters I through VII apply (Bankruptcy Act section 102, 11 U.S.C. 502). The Court concluded that the date of adjudication was the date of the approval of the petition for reorganization.

The petition was filed on October 3, in the District Court of New York and was approved that same day. Subsequently, from October 4 to October 10, the defendant, a Louisiana bank, honored checks totaling approximately $7,000 without actual knowledge of the bankruptcy.

attention and none have been found interpreting the meaning or purpose of this provision, the matter must be considered res integra. When the bankruptcy occurs the bank upon which the bankrupt drew a check prior to the date of the bankruptcy finds himself caught in the intermeshing of two highly complicated systems of law. Traditionally, it is the primary function of the Bankruptcy Act to protect the creditors, to marshal the assets, and to distribute them among the creditors equitably and ratably in accordance with their respective rights and interests. Negotiability tries to give the bank the maximum assurance that it will be able to cash the check without any defenses being interposed. An expansion of bankruptcy in some senses indisputably hinders the flow of commercial paper. *In the absence of any prior interpretation, we agree with counsel for defendants that one of the purposes of the 'negotiability' provision in the Bankruptcy Act was to protect a bank in a case of this kind, if the bank was in good faith and had no 'actual knowledge' of the pending bankruptcy."* (*Rosenthal v. Guaranty Bank and Trust Company* (D.C. La. 1956) 139 F.Supp. 730 at 734; emphasis added.)

The Court in *Rosenthal*, in addition to determining that the negotiability proviso of section 70d(5) was intended to protect drawee banks, held that it applied to transfers occurring after adjudication.[5] No reason

[5]The checks that were honored by the bank in *Rosenthal v. Guaranty Bank and Trust Company* (D.C. La. 1956) 139 F.Supp. 730 were honored after adjudication.

Although the technical adjudication of bankruptcy for the purposes of corporate reorganization did not occur for almost

exists for distinguishing between transfers occurring before or after adjudication insofar as section 70d(5) is concerned. The very language of the negotiability proviso of section 70d(5) indicates that it is not to be restricted by any other provision in the Act. The proviso does not appear in the introductory language of section 70d(5), but as a qualification to section 70d(5), which deals with all transfers occurring after bankruptcy. Since transfers occurring either prior or subsequent to adjudication fall into this category, the negotiability proviso applies in either situation.

The negotiability proviso of section 70d(5) protects the Bank of Marin in honoring the checks of its depositor, Marin Seafoods, under the facts of this case. Any other interpretation of that section would distort the plain meaning of the terms used and the obvious intent of Congress in enacting such a provision.

---

three years after the filing of the petition, the Court in *Rosenthal* considered the date of the filing of the petition as the date of adjudication for the purpose of interpreting Bankruptcy Act section 70a and for determining the issue presented.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment of the Court of Appeals for the Ninth Circuit be reversed and the cause remanded to the District Court for entry of the appropriate order in favor of the Bank of Marin.

Dated, San Rafael, California,
July 20, 1966.

CARLOS R. FREITAS,
BRYAN R. MCCARTHY,
EDGAR B. WASHBURN,
FREITAS, ALLEN, MCCARTHY & BETTINI,
Counsel for Petitioner.

(Appendix Follows)

BLANK

PAGE

Appendix

United States Constitution Amendment V:

No person shall be . . . deprived of life, liberty or property without due process of law.

Bankruptcy Act section 18(f), 73 Stat. 109 (1959), 11 U.S.C. 41(f):

The filing of a voluntary petition under chapters 1 to 7 of this title, other than a petition filed in behalf of a partnership by less than all of the partners, shall operate as an adjudication with the same force and effect as a decree of adjudication.

Bankruptcy Act section 70, 52 Stat. 879-881 (1938) as amended, 11 U.S.C. 110: Title to property:

(a) The trustee of the estate of a bankrupt and his successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located . . . property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him or otherwise seized, impounded, or sequestered. . . .

. . .

(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

. . .

(1) A transfer of any of the property of the bankrupt, other than real estate, made to a person acting in good faith shall be valid against the trustee if made for a present fair equivalent value or, if not made for a present fair equivalent value, then to the extent of the present consideration actually paid therefor, for which amount the transferee shall have a lien upon the property so transferred;

(2) A person indebted to the bankrupt or holding property of the bankrupt may, if acting in good faith, pay such indebtedness or deliver such property, or any part thereof, to the bankrupt or upon his order, with the same effect as if the bankruptcy were not pending;

(3) A person having actual knowledge of such pending bankruptcy shall be deemed not to act in good faith unless he has reasonable cause to believe that the petition in bankruptcy is not well founded;

(4) The provisions of paragraphs (1) and (2) of this subdivision shall not apply where a receiver or trustee appointed by a United States or State court is in possession of all or the greater portion of the non-exempt property of the bankrupt;

(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision g of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: Provided, however, That nothing in this title shall impair the negotiability of currency or negotiable instruments.

. . .

BLANK

PAGE

AMICUS CURIAE BRIEF

BLANK

PAGE

In the Supreme Court of the United States

October Term, 1965

No[redacted] 63

Bank of Marin,
Petitioner,
vs.
John M. England, Trustee in Bankruptcy,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

Brief of California Bankers Association, Amicus Curiae, in Support of Petitioner

John P. Austin
Paul E. Homrighausen
Thomas A. Lee, Jr.
Morrison, Foerster, Holloway, Clinton & Clark
120 Montgomery Street
San Francisco, California
Counsel for the Amicus Curiae

SORG PRINTING COMPANY OF CALIFORNIA. 346 FIRST STREET. SAN FRANCISCO 94105

BLANK

PAGE

SUBJECT INDEX

	Page
Statement of Interest of the Amicus Curiae	1
Summary of Argument	2
Argument	3
A. The Failure of the Trustee to Revoke the Bankrupt's Order for the Payment of Funds on Deposit with the Petitioner or to Give Notice of the Bankruptcy Proceeding Bars the Trustee from Recovery Against the Petitioner	3
B. Even Assuming That Payment of the Checks in Question Constituted an Invalid Transfer as Against the Respondent, Recovery Should Not Be Permitted Against the Petitioner	8
Conclusion	12

TABLE OF AUTHORITIES CITED

Cases	Pages
Anderson Nat'l Bank v. Luckett, 321 U.S. 233, 248 (1944)	4, 5
Basch v. Bank of America Nat'l Trust & Sav. Ass'n., 22 C.2d 316, 321, 139 P.2d 1 (1943)	4, 5
Citizens Union Nat'l Bank v. Johnson, 286 Fed. 527 (6th Cir. 1923)	7, 10
Christensen v. Felton, 322 F.2d 323 (9th Cir. 1963)	4
Dix v. Bank of California Nat'l Ass'n., 113 F. Supp. 823, 825 N.D. Cal. 1952), *aff'd sub nom.* Dix v. Pineda, 205 F.2d 957 (9th Cir. 1953)	4
Guthrie Nat'l Bank v. Gill, 6 Okla. 560, 54 Pac. 434 (1898)	6, 7
Harrison State Bank v. First Nat'l Bank, 116 Neb. 456, 218 N.W. 92 (1928)	6
Hummel v. Equitable Life Assur. Soc., 151 F.2d 994 (7th Cir. 1945)	4
In re American Foam Rubber Corp., 222 F. Supp. 679 (S.D. N.Y. 1963)	10
In re Howe, 235 Fed. 908 (D. Mass. 1916), *aff'd sub nom.* Edison Elec. Illuminating Co. v. Tibbetts, 241 Fed. 468 (1st Cir. 1917)	8, 12
In re Woodruff, 272 F.2d 696, 699 (7th Cir. 1959)	3
Rosenthal v. Guaranty Bank & Trust Co., 139 F. Supp. 730 (D.C. La. 1956)	7, 9
Schultz v. England, 106 F.2d 764, 768 (9th Cir. 1939)	3, 4
Zartman v. First Nat'l Bank, 216 U.S. 134, 138 (1910)	3

STATUTES Pages

Bankruptcy Act:

Section 18(f), 11 U.S.C. 41(f) 10
Section 63(a), 11 U.S.C. 103(a) 11
Section 70(a), 11 U.S.C. 110(a) 3
Section 70(d), 11 U.S.C. 110(d) 8, 10
Section 70(d)(5), 11 U.S.C. 110(d)(5) 2, 3, 8

California Financial Code, Section 990 5
California Uniform Commercial Code, Section 4403 5

TEXTS

Brady, Bank Checks (3d ed.) 5, 6, 7
4 Collier, Bankruptcy (14th ed.) 3, 9

MISCELLANEOUS

H.R. Rpt. No. 1409, 75th Cong., 1st Sess. 35 (1937) 9
National Bankruptcy Conference, Analysis of H.R. 12889, 74th Cong., 2d Sess., 229-31 (1936) 9

BLANK

PAGE

In the Supreme Court of the United States

October Term, 1965

No. 950

Bank of Marin,
Petitioner,
vs.
John M. England, Trustee in Bankruptcy,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

Brief of California Bankers Association, Amicus Curiae, in Support of Petitioner

---

By consent of petitioner, Bank of Marin, and of respondent, John M. England, Trustee in Bankruptcy, filed herewith, the California Bankers Association files this brief as amicus curiae in support of petitioner.

STATEMENT OF INTEREST OF THE AMICUS CURIAE

The amicus curiae, the California Bankers Association, is a nonprofit California corporation, the membership of which is composed of commercial banks operating in the State of California. It is interested in this litigation for

the following reasons: The United States Court of Appeals for the Ninth Circuit has held that a bank which honors checks of one of its depositors after that depositor has filed a voluntary petition in bankruptcy is liable to the Trustee in Bankruptcy for the amount of those checks, although the bank made payment in good faith and without notice of the bankruptcy proceeding. Since banks are under a legal obligation to honor checks of their depositors duly presented, and since it is impossible for banks to keep themselves currently advised of all petitions in bankruptcy affecting their depositors, affirmance of that ruling would result in great and unprotectable loss to the banking industry in California.* Accordingly, this litigation is of vital interest to the banks of this State.

SUMMARY OF ARGUMENT

The amicus curiae agrees with and supports each argument advanced by the petitioner in its opening brief. In order to supplement petitioner's argument and to avoid repetition, the amicus curiae will restrict its brief to the following two arguments:

First: Upon the filing of a petition in bankruptcy, the Trustee in Bankruptcy succeeds only to such rights as are possessed by the bankrupt. In this case, the bankrupt would have been entitled to recover the amount of the checks which petitioner honored pursuant to its order only if it had revoked that order prior to the time of payment. Since no such "stop payment" order (or notice of the bankruptcy proceeding) was given, the trustee, as the bankrupt's successor, is also barred from recovery.

Second: Even if payment of those checks constituted a transfer rendered invalid by Section 70(d)(5) of the

---

*For discussion of the extent of that loss, see p. 9, *infra*.

Bankruptcy Act (11 U.S.C. § 110(d)(5)), that provision does not require this Court to hold *both* petitioner and the payee of the checks liable to the trustee. In equity and in fairness, it should not do so.

ARGUMENT

A. The Failure of the Trustee to Revoke the Bankrupt's Order for the Payment of Funds on Deposit with the Petitioner or to Give Notice of the Bankruptcy Proceeding Bars the Trustee from Recovery Against the Petitioner

In granting recovery to the Trustee, the courts below relied on Section 70(a) of the Bankruptcy Act, (11 U.S.C. § 110(a)). This section provides in part:

> "The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, . . . to . . . (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred. . . ."

Under that provision a trustee in bankruptcy succeeds *only* to such rights as the bankrupt possessed at the time of the filing of the bankruptcy petition, and is subject to all claims, defenses and equities which might have been asserted against the bankrupt but for the filing of that petition.

Zartman v. First Nat'l Bank, 216 U.S. 134, 138 (1910);

In re Woodruff, 272 F.2d 696, 699 (7th Cir. 1959);

Schultz v. England, 106 F.2d 764, 768 (9th Cir. 1939);

4 Collier, *Bankruptcy,* p. 1244 (14th ed.).

Thus, for example, where a trustee asserts a claim based upon a contract between the bankrupt and a third party, the trustee's rights against that third party depend upon the terms of the contract and are no greater than those which the bankrupt might have exercised thereunder.

See,

> *Christensen v. Felton,* 322 F.2d 323 (9th Cir. 1963);
> *Hummel v. Equitable Life Assur. Soc.,* 151 F.2d 994 (7th Cir. 1945);
> *Schultz v. England, supra.*

Accordingly, in determining whether the trustee in this case is entitled to recover from petitioner, it is first necessary to ascertain the nature and extent of the rights of the bankrupt against the petitioner.

It is well established both in California and elsewhere that an ordinary depositor does not have title to any specific funds which he deposits in a bank: the relationship of bank and depositor is that of debtor and creditor, and is founded upon contract.

See,

> *Anderson Nat'l Bank v. Luckett,* 321 U.S. 233, 248 (1944);
> *Dix v. Bank of California Nat'l Ass'n.,* 113 F. Supp. 823, 825 (N.D. Cal. 1952), *aff'd sub nom. Dix v. Pineda,* 205 F.2d 957 (9th Cir. 1953);
> *Basch v. Bank of America Nat'l Trust & Sav. Ass'n.,* 22 C.2d 316, 321, 139, P.2d 1 (1943).

Under that contract, a bank has the right and the duty to honor checks of its depositor properly drawn and duly presented.

See,

Anderson Nat'l Bank v. Luckett, supra;

Basch v. Bank of America Nat'l Trust & Sav. Ass'n., supra;

Brady, *Bank Checks,* § 12.3 (3d ed.).

The depositor may revoke his order for payment from his account by giving the bank notice thereof prior to the time his checks are accepted or paid by the bank.

See,

California Financial Code § 990;*

Brady, *op. cit. supra,* §§ 10.7, 13.1, 13.3.

But absent revocation by a timely "stop payment" notice, payment by the bank operates to discharge its obligation under that contract, and the depositor has no right to recover the amounts paid.

See,

Basch v. Bank of America Nat'l Trust & Sav. Ass'n., supra;

Brady, *op. cit. supra,* §§ 10.7, 10.8, 13.1, 13.3.

The applicability of those basic principles to the facts of this case is self apparent. Prior to the filing of its voluntary petition in bankruptcy, Marin Seafoods, Inc., drew checks totaling the sum of $2,312.82 upon the petitioner, with which it had a commercial account (R. 45-46); the checks were drawn in favor of a creditor of the bankrupt, Eureka Seafoods, and were outstanding on September 26, 1963, the date of the filing of that petition (R. 46). Those checks were honored by the petitioner on October 2, 1963 (R. 46).

---

*This statute was repealed as of January 1, 1965, with the adoption of the Uniform Commercial Code in California. Section 4403 of the Uniform Commercial Code embodies the same principle.

At no time on or before that date did the bankrupt or the Trustee in Bankruptcy revoke the bankrupt's order for payment of those checks or inform the petitioner of the bankruptcy proceeding. (R. 47.) Under these circumstances, the bankrupt would have had no right to recover the amount of those checks from the petitioner. Accordingly, the Trustee is also barred from recovery, and the lower court's judgment should be reversed accordingly.

The Court of Appeals below rejected the foregoing contention on the ground that:

> "The bankruptcy of a drawer operates as a revocation of the drawee's authority. Such revocation is not dependent upon or subject to notice of the drawee, since the trustee is immediately vested with the title of the bankrupt by operation of law. . . . These circumstances constitute an implied exception to the contractual obligation of the bank to honor checks unless and until a 'stop payment' notice is received." (352 F.2d at 191 (R. 113).)

In support of its conclusion that the bankruptcy of a drawer operates as a revocation of the drawee's authority, the court cited the following authorities: *Harrison State Bank v. First Nat'l Bank,* 116 Neb. 456, 218 N.W. 92 (1928); *Guthrie Nat'l Bank v. Gill,* 6 Okla. 560, 54 Pac. 434 (1898); and Brady, *Bank Checks,* p. 25 (3d ed.). The amicus curiae submits that none of those authorities support that conclusion: all are consistent with the general principles set forth above.

Harrison State Bank v. First Nat'l Bank, supra, involved an action against a drawee bank which had refused to honor drafts by one of its depositors, a second bank, *after it had received notice* that the depositor was insolvent and had been ordered closed by the Comptroller of the Cur-

rency. The Nebraska Supreme Court merely held the defendant not liable to the payee of those drafts for having refused payment after receipt of such notice.

In *Guthrie Nat'l Bank v. Gill, supra,* defendant bank had refused to honor a check *where it had notice* that after the check was drawn the drawer had made an assignment for the benefit of the creditors. Here, again, the court simply ruled that the defendant was not liable to the payee for having refused payment.

Brady, *Bank Checks,* p. 25 (3d ed.), merely cites the same two inapposite cases as authority for the statement that:

> "In the absence of statute, bankruptcy or insolvency of a drawer of checks operates as a revocation of authority of the drawee bank to pay uncertified checks outstanding."

However, Brady continues as follows:

> "A bank has been held liable in paying a check issued after the drawer made an assignment for the benefit of creditors, where the bank *had knowledge* of drawer's insolvency, even though the check was dated prior to the assignment. *But a bank paying a check in good faith in ignorance of drawer's bankruptcy or insolvency is protected in its payment."* (Emphasis added.)

For the latter proposition, Brady cites two cases, *Citizens Union Nat'l Bank v. Johnson,* 286 Fed. 527 (6th Cir. 1923) and *Rosenthal v. Guaranty Bank & Trust Co.,* 139 F. Supp. 730 (D.C. La. 1956). Both of those cases, considered in the brief of the petitioner, lend additional support to the view that a bank fulfilling its contractual obligation to its depositor without notice of his bankruptcy is entitled to protection under the law.

See also,

In re Howe, 235 Fed. 908 (D. Mass. 1916), *affirmed sub nom. Edison Elec. Illuminating Co. v. Tibbetts*, 241 Fed. 468 (5th Cir. 1917).

B. Even Assuming That Payment of the Checks in Question Constituted an Invalid Transfer as Against the Respondent, Recovery Should Not Be Permitted Against the Petitioner

The Court of Appeals below also based its decision upon the ground that payment of the bankrupt's checks after the filing of its voluntary petition constituted a transfer which is invalid against the respondent under Section 70(d)(5) of the Bankruptcy Act (11 U.S.C. § 110(d)(5)). That section provides in part as follows:

> "Except as otherwise provided in this subdivision and in subdivision g of Section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee . . ."

The amicus curiae believes that this contention has been adequately answered by the brief of the petitioner and in the preceding section of this brief. For the purposes of argument, however, the amicus curiae will assume that the payment of those checks did constitute such a transfer. Even on that assumption, petitioner should not be held jointly liable with the payee of those checks.

Prior to the enactment of Section 70(d), there was considerable confusion in the cases as to which of those transactions occuring between the filing of a petition in bankruptcy and adjudication were to be protected against the claims of the trustee. Section 70(d) was enacted to end that confusion by specifically designating certain transactions entitled to protection.

See,

H.R. Rpt. No. 1409, 75th Cong., 1st Sess. 35 (1937); National Bankruptcy Conference, Analysis of H.R. 12889, 74th Cong., 2d Sess., 229-31 (1936); 4 Collier, *op. cit, supra,* para. 70.66, 70.67.

But there is nothing in the language or the legislative history of that provision which compels this Court to rule that the trustee is entitled to judgment against both the transferee-payee of those checks and the transferor-bank. For the reasons set forth below, it is submitted that the Court should not do so in this case.

That there is no equitable basis for permitting recovery against the petitioner can scarcely be disputed. Petitioner paid out the amounts in question in good faith, and in reliance upon its contractual obligation to honor checks of its depositor. At the time it did so, petitioner had no notice whatever of the bankruptcy proceeding (R. 47), although the respondent was aware of the bankrupt's account with the petitioner and could very easily have provided such notice (R. 2, 9, 46). Since it is obviously impossible for banks to keep themselves informed hour by hour of the filing of all voluntary petitions in every district court in every state which may affect their depositors, affirmance of the lower court's judgment would render banks subject to repeated and substantial judgments against which they have no effective means of protection.*

The justification for imposing liability on the payee of those checks is readily apparent. Eureka Fisheries is an

*The Court of Appeals below recognized the bank's "dilemma" and the "hardship and impracticability" of "timely discovery of bankruptcy proceedings involving [a bank's] depositors." (352 F.2d at 190 (R. 111.)) But it went on to suggest that since *Rosenthal v. Guaranty Bank & Trust Co.,* 139 F. Supp. 730 (D.C. La. 1956), is the only previously reported case dealing with the question presented herein, that question is not one which will

unsecured trade creditor of the bankrupt, to which the bankrupt was indebted for merchandise delivered (R. 12). In its dealings with the bankrupt it voluntarily assumed the risks incident to a credit relationship, including the risk of bankruptcy. Yet, by reason of the transfers involved herein, that creditor received payment of its claims after its debtor had filed a petition in bankruptcy. Requiring that creditor to pay the trustee the amount of the funds

---

frequently confront banks and, therefore, does not threaten banks with great financial loss. That inference is mistaken.

Prior to the enactment of the present Section 18(f) (11 U.S.C. 41(f)) of the Bankruptcy Act in 1959, there was an interval between the date of the filing of both a voluntary and an involuntary petition and the adjudication of bankruptcy. At the time of that enactment it was well settled that a bank honoring checks of its depositor during that interval without notice of a bankruptcy proceeding affecting that depositor was entitled to protection against the claims of a trustee. See, Bankruptcy Act, § 70(d) (11 U.S.C. 110 (d)); *Citizens National Bank v. Johnson,* 286 Fed. 527 (6th Cir. 1923); *In re American Foam Rubber Corp.,* 222 F. Supp. 679 (S.D. N.Y. 1963). That interval provided banks with an opportunity to become advised of the pendency of the bankruptcy proceeding prior to adjudication and to protect themselves accordingly. For that reason, the question presented herein did not arise.

As enacted in 1959, Section 18(f) of the Bankruptcy Act eliminated that interval in the case of voluntary petitions by making the time of adjudication coincidental with the filing of the petition in bankruptcy. Nonetheless, it was generally assumed by banks and trustees in bankruptcy alike that that enactment was not intended to and did not operate to deprive banks of the protection which has theretofore been afforded. *Rosenthal v. Guaranty Bank & Trust Co., supra,* lent support to that assumption.

Since the decision of the District Court below in 1964, however, trustees have with increasing frequency asserted claims similar to those asserted by the respondent herein. The amicus curiae has been advised by one of its members, Bank of America National Trust & Savings Association, that since that time such claims have been asserted against it in six voluntary bankruptcy proceedings. Other banks operating in this State have reported similar experiences since the date of that decision. Given these considerations, and the large and increasing number of voluntary petitions in bankruptcy filed in this State, and throughout the country, every day, affirmance of the lower court's judgments would inevitably result in a very substantial loss to the banking industry.

so received would place it in no worse a position than before those transfers: It would merely be deprived of what amounts to a preferential payment of its claims and restored to its proper position as a general creditor of the bankrupt.

Imposition of liability upon the petitioner would have very different consequences. The petitioner was not a creditor of the bankrupt prior to its bankruptcy, and did not undertake the risks of a creditor in dealing with the bankrupt. The petitioner has received no benefit whatever from the transactions involved herein, but has merely paid out funds in satisfaction of its contractual obligation to one of its depositors. Accordingly, a judgment against petitioner would not deprive it of a benefit obtained at the expense of other creditors of the bankrupt, nor restore it to its prior position vis a vis the bankrupt.* Rather, as noted in the brief of the petitioner, such a judgment would result in the petitioner's having to pay the same debt twice.†

If this were a case in which the Court had to decide which of two innocent parties, the bank or the general creditors of the bankrupt, must ultimately bear the consequences of the bankrupt's action, it may be that the loss should fall upon the bank. But this is not such a case. Similarly, if the trustee had notified the petitioner of the bankruptcy pro-

---

*Petitioner would not even have a provable claim against the bankrupt's estate, since it arose after adjudication. See Bankruptcy § Act 63(a) (11 U.S.C. § 103(a)). And any claim of the petitioner against its bankrupt corporate depositor apart from bankruptcy would be worthless.

†Eureka Fisheries has satisfied the joint judgment rendered by the District Court below against it and the petitioner, but it has also filed a claim for contribution against the petitioner in the bankruptcy court (R. 54-55). Regardless of the merits of that claim this Court, in the exercise of its equitable powers, should reverse the lower court's judgment to avoid unnecessary circuity and multiplicity of action.

ceeding promptly, as it could easily have done, imposition of liability upon the petitioner might be justified. But the trustee failed to do so. It is therefore submitted that the Court should protect both the petitioner and those general creditors, and permit the trustee to obtain recovery only against that party which benefited from the subject transactions.

Support for the position of the amicus curiae is found in *In re Howe*, 235 Fed. 908 (D. Mass. 1916), *affirmed sub nom. Edison Elec. Illuminating Co. v. Tibbetts*, 241 Fed. 468 (1st Cir. 1917), a case involving facts closely parallel to that involved herein. There, both courts recognized that the payment of checks of a bankrupt following an adjudication of bankruptcy constituted an invalid transfer as against the trustee, and held the trustee entitled to recover the value of those checks from the payee. But the courts also recognized that despite the invalidity of that transfer, the trustee might be denied recovery in a suit against the drawee bank.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment of the Court of Appeals for the Ninth Circuit should be reversed.

Dated: August 19, 1966.

John P. Austin
Paul E. Homrighausen
Thomas A. Lee, Jr.
Morrison, Foerster, Holloway,
Clinton & Clark
Counsel for the Amicus Curiae

BLANK

PAGE